



# Arizona State Senate *Issue Brief*

September 22, 2006

## **Note to Reader:**

The Senate Research Staff provides nonpartisan, objective legislative research, policy analysis and related assistance to the members of the Arizona State Senate. The *Research Briefs* series, which includes the *Issue Brief*, *Background Brief* and *Issue Paper*, is intended to introduce a reader to various legislatively related issues and provide useful resources to assist the reader in learning more on a given topic. Because of frequent legislative and executive activity, topics may undergo frequent changes. Additionally, nothing in the *Brief* should be used to draw conclusions on the legality of an issue.

## **ARIZONA'S DIRECT SHIPMENT OF ALCOHOLIC BEVERAGES**

### **INTRODUCTION**

The passage of the 21<sup>st</sup> Amendment to the U.S. Constitution, which repealed prohibition, gave states complete authority to regulate the importation, distribution and sale of alcoholic beverages. Two main types of regulatory schemes evolved after the change: control states and license states.

Control states control all aspects of beverage distribution and sale. States buy from the licensed manufacturer, then store, distribute and sell the product. The states collect the sales and excise taxes in state-run stores. License states, including Arizona, license all aspects of private production, distribution and sales. License states have set up a hierarchical business licensing system known as the three-tier system. Under such a system, all alcohol must move from supplier to wholesaler to retailer, rather than directly to the consumer. The state maintains control through the approval and sale of licenses as well as the oversight of licensees' business practices and collection of taxes. In Arizona, the Department of Liquor Licenses and Control (Department) regulates all licensees within the three-tier system.

Changes in the beverage industry have led to modifications in the two schemes, creating hybrid systems. Some control states have granted exemptions from state control for farm wineries, brew-pubs and bed-and-breakfasts. The allowance of reciprocal wine shipping laws and the granting of limited exemption for shipping and transporting of personal use have also modified the two schemes.

According to the National Conference of State Legislatures, the growth of direct shipping has caused concern in some states, including Arizona, because direct shippers can:

- avoid state sales and excise taxes.
- bypass the state-sanctioned three-tier systems of production, wholesaling and retail sales.
- ship beverages illegally to "dry" jurisdictions and minors.
- create an unfair business environment in which only in-state

businesses must comply with state regulations.

- Reduce states' powers to regulate alcoholic beverages within their borders.

## **HISTORY OF DIRECT SHIPMENT IN ARIZONA**

**1999** - To address concerns related to direct shipping in Arizona, legislation was enacted in 1999 to establish a direct shipment license and define a three-tiered system for out-of-state producers (Laws 1999, Chapter 155). Pursuant to the legislation, an out-of-state producer licensed as a direct shipper is required to deliver the spirituous liquor to a wholesaler licensed in this state. The wholesaler is required to pay all luxury taxes and deliver the liquor to a licensed retailer with off-sale privileges. Finally, the retailer is required to pay all transaction privilege taxes and ensure that delivery occurs during hours when liquor is legally sold in this state, to a person 21 years of age or older and who exhibits proper identification. The legislation also requires the retailer to keep a record of the time, date, delivery type and amount of the shipment and the name, address, signature and identification number of the consumer. The direct shipment licensee is liable for any violation of liquor statutes. The direct shipment licensee may be served a cease and desist order for a violation and charged a civil penalty by the Director of the Department of Liquor Licenses and Control of not more than \$150,000 for knowingly violating the order.

**2002** - In 2002, interest was expressed regarding the ability to ship wine directly home to Arizona from out-of-state winery visits without having to go through the required three-tiered system. Legislation was enacted to allow a consumer to arrange for shipment of one case of wine annually to the consumer's residence by a common carrier when the consumer purchases the wine at the physical location of the winery in the other state (Laws 2002, Chapter 155).

**2003** - In 2003, some Arizonans expressed their desire to be able to shop for wine at Arizona wineries and have that wine shipped directly home from the in-state winery. Laws 2003, Chapter 161, allows for the direct

shipment of wine from an in-state winery to a residential address and increases the amount that may be shipped from any winery, from one case to two cases of wine per winery per year. The legislation restricts the wine to personal use only and requires the wine to be marked to require an adult's signature on delivery.

**2005** - In 2005, the direct shipment requirements were clarified to state that purchasers wishing to ship directly to themselves from a winery must be able to have carried the wine lawfully into or within Arizona (Laws 2005, Chapter 284).

Other states also passed legislation to address direct shipment concerns. Over the years, the wine industry questioned whether state laws can treat an in-state winery different from an out-of-state winery. In 2005, the United States Supreme Court struck down Michigan's and New York's direct shipment laws because they discriminated against interstate commerce in violation of the Commerce Clause of the Constitution of the United States. In *Granholm v. Heald*, 125 S. Ct. 1885 (2005), the Court held that this discrimination was not authorized by the 21<sup>st</sup> Amendment to the U.S. Constitution.

**2006** - In response to concern that Arizona's direct shipment statutes treat out-of-state and in-state direct wine sales in a different fashion, the domestic farm winery license was modified in 2006. A domestic farm winery is defined to include any winery in the United States that meets the statutory requirements. Additionally, domestic farm wineries no longer need to have 75 percent of their grapes grown in Arizona. Finally, domestic farm wineries may ship directly to consumers and to retailers if the winery produces less than 20,000 gallons of wine annually (Laws 2006, Chapter 310).

## **ADDITIONAL RESOURCES**

- Arizona Department of Liquor Licenses and Control  
800 W. Washington, 5th floor  
Phoenix, AZ 85007  
602-542-5141  
[www.azll.com](http://www.azll.com)
- Goehring, Jan. "Courts Unplug the Wine Debate." *State Legislatures*. June 2001

- Frohling, Robert and Kurtz, Karl. "Direct Shipments of Alcoholic Beverages to Consumers." Vol. 6, No. 10. February 1998 [www.ncsl.org](http://www.ncsl.org).
- Boulard, Garry. "Wine Wars: To Ship or Not to Ship." *State Legislatures*. October/November 1997
- Gray, C. Boyden. "21st Amendment Grants States Unique Authority to Regulate Distribution of Alcohol." *Washington Legal Foundation*. March 17, 2000
- "Possible Anticompetitive Barriers to E-Commerce: Wine." Staff of the Federal Trade Commission. July 2003
- Wine Institute  
[www.wineinstitute.org](http://www.wineinstitute.org)
- Coalition for Free Trade  
<http://www.coalitionforfreetrade.org/>
- Free the Grapes  
[www.freethethegrapes.org](http://www.freethethegrapes.org)
- Direct Shipment Liquor Statutes: Arizona Revised Statutes, Title 4